

Message Text

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ACTION EA-12

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UNCLAS TAIPEI 05446

E.O. 11652: N/A
TAGS: EFIN, TW
SUBJECT: US DOLLAR FORWARD MARKET OFF TO A SLOW START

1. AFTER 4 DAYS OF OPERATION, TRANSACTIONS IN THE NEW US DOLLAR FORWARD MARKET ARE AT A LOW LEVEL, AROUND US\$20 - US\$30 MILLION PER DAY, ACCORDING TO CENTRAL BANK OF CHINA (CBC) ESTIMATES, WITH EXPORTERS ACCOUNTING FOR MOST OF THE BUSINESS. A CBC OFFICIAL TOLD EMBASSY THAT THE SLOW START WAS DUE TO (1) TRADERS' LACK OF FAMILIARITY WITH THE MARKET, AND (2) THE VERY SLIGHT DIFFERENCE BETWEEN THE PRESENT AND 180-DAY RATES, WHICH MAY LEAD TRADERS TO BELIEVE THAT THERE WILL BE NO SUBSTANTIAL REVALUATION IN THE NEXT FEW MONTHS.
2. BANKERS HERE REPORT THAT LACK OF BUSINESS IS ALSO CAUSED BY HIGH COST TO EXPORTERS OF SELLING DOLLARS FORWARD -- EXPORTERS MUST NOT ONLY TAKE A SLIGHT LOSS OVER THE PRESENT RATE, BUT MUST ALSO FOREGO INTEREST ON THE 5 PERCENT DEPOSIT REQUIRED. SEVERAL US BANKERS TOLD EMBASSY THAT PRE-EXPORT LOAN VOLUMES HAVE INCREASED SUBSTANTIALLY SINCE THE JULY 11 REVALUATION, AND THEY EXPECT THAT MANY EXPORTERS WILL CONTINUE TO UTILIZE THESE LOANS TO "COVER"

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THEMSELVES AGAINST ANY FUTURE REVALUATION OF THE NT DOLLAR, RATHER THAN GO INTO THE FUTURES MARKET. PRE-EXPORT LOANS ARE GRANTED IN US DOLLARS, CONVERTED INTO NT AT THE CURRENT RATE BY THE BORROWER, AND THEN PAID OFF IN SIX MONTHS OR SO IN THE EXPORT PROCEEDS, US DOLLARS.

3. COMMENT: EXPORTERS WILL PROBABLY MAKE GREATER USE OF

THE US FORWARD MARKET AS THEY BECOME MORE FAMILIAR WITH ITS OPERATIONS. COVERING BY USE OF PRE-EXPORT LOANS EXHAUSTS LINES OF CREDIT WHICH MAY BE BETTER SUITED FOR OTHER PURPOSES.

4. BANKERS REPORT THAT IMPORTERS, WHO FEEL THAT ANY EXCHANGE RATE ADJUSTMENT WILL BE FAVORABLE TO THEIR INTERESTS, ARE ONLY PURCHASING 30-DAY FUTURE CONTRACTS, BECAUSE THEY OBTAIN A BETTER EXCHANGE RATE. THE SPOT RATE FOR BUYING US DOLLARS IS 36.05, WHILE THE FORWARD RATE FOR ONE TO 30 DAYS IS 35.9. WHILE EUROPEAN FORWARD MARKETS PROVIDE FOR SETTLEMENT ON A SPECIFIC DAY (E.G. 30 DAYS FROM THE AGREEMENT), THE CBC CONTRACT PROVIDES FOR SETTLEMENT AT ANY TIME BETWEEN ONE AND 30 DAYS AFTER (OR 31 TO 60 DAYS; 61 TO 90 DAYS; ETC., DEPENDING ON THE FORWARD PERIOD). CONSEQUENTLY, SOME IMPORTERS HAVE SETTLED THEIR CONTRACTS AFTER ONLY TWO OR THREE DAYS, PURCHASING US DOLLARS FOR 35.9 NT EACH, THUS MINIMIZING LOSSES DUE TO THE NON-INTEREST BEARING 5 DEPOSIT. THE CBC IS NOW ALERT TO THIS PRACTICE, AND MAY REVISE THE MARKET REGULATIONS TO PREVENT IT.

5. RUMORS OF ANOTHER REVALUATION CONTINUE TO CROP UP. CENTRAL BANK OFFICIALS ARE CLOSE-MOUTHED, AS USUAL; DEPUTY GOVERNOR LIANG TOLD EMBOFF THAT THE RAPID ESTABLISHMENT OF THE FORWARD MARKET DID "NOT NECESSARILY" MEAN THE UNCLASSIFIED

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NT WOULD SOON BE REVALUED. UNGER

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